Virginia Tax Bulletin

Virginia Department of Taxation

January 4, 1999 **99-1**

Personal Property Tax Relief Act of 1998: Income Tax Treatment of Tax Relief

The Personal Property Tax Relief Act of 1998 (the "Act") was passed by the General Assembly and is now law. Beginning in 1998, the tax on the first $20,000 of the value of cars, pick-up or panel trucks (weighing 7,500 pounds or less), and motorcycles owned or leased for personal use will be incrementally reduced. The personal property tax on cars, pick-up or panel trucks (weighing 7,500 pounds or less), and motorcycles will be reduced by 12.5% of the tax on the first $20,000 of value on qualifying vehicles in 1998, 27.5% in 1999, 47.5% in 2000, 70% in 2001, and 100% in 2002. These tax reductions are calculated using a locality's personal property tax rates in effect on August 1, 1997. Beginning in 1998, however, for qualifying vehicles valued at $1,000 or less, the tax reduction is equal to 100% of the tax, also based on the local tax rates in effect on August 1, 1997.

For 1998 tangible personal property taxes, the tax relief will be in the form of a refund from the Commonwealth to the taxpayer. For 1999 tangible personal property taxes and thereafter, the tax relief will take the form of a reduction of the tax due, which will be displayed on the taxpayer's personal property tax bill. The taxpayer will only be responsible for paying the personal property tax shown as due on the bill.

The Commonwealth requested a private letter ruling from the Internal Revenue Service (IRS) regarding the tax implications of the Act. On September 30, 1998, the IRS issued its ruling, LTR 98-114289 (Sept. 30, 1998), to the Commonwealth.

Generally speaking, the tax relief granted by the Act does not result in taxable income to the recipients. However, in situations where an individual has been refunded personal property tax which was previously reported as an itemized deduction, the individual will be required to include the refund in income to the extent they previously received a tax benefit. The purpose of this bulletin is to explain the income tax implications of the Act pursuant to the IRS ruling.

1998 Refunds of 1998 Taxes Paid in 1998

Taxpayers who paid their 1998 personal property tax between January 1, 1998 and June 30, 1998, should have received a refund check by November 15, 1998. Also, some taxpayers who paid their 1998 personal property taxes on or after July 1, 1998, may receive a refund prior to January 1, 1999.

Those taxpayers who will claim the standard deduction and who will not itemize deductions on their 1998 federal income tax return ("Non-itemizers") should not include the amount of their 1998 personal property tax refunds of 1998 taxes when reporting income on their 1998 federal or Virginia income tax returns. In short, non-itemizers have no federal or state income tax reporting responsibilities with respect to their personal property tax refunds.

Those taxpayers who will not claim the standard deduction and who will itemize deductions on their 1998 federal income tax return ("Itemizers") must subtract the amount of their 1998 personal property tax refund received in 1998 from the total amount of personal property tax they have paid in 1998. Itemizers can deduct this net amount as an itemized deduction on their 1998 federal income tax returns, the result of which will flow through to the income reported on itemizers' 1998 Virginia income tax returns.

1999 Refunds of 1998 Taxes Paid in 1998

Taxpayers who pay their 1998 personal property tax between July 1, 1998 and December 31, 1998, most likely will receive their refund check in 1999, no later than May 15.

Those taxpayers who were non-itemizers in 1998 should not include the amount of their personal property tax refunds received in 1999 when reporting income on their 1999 federal or Virginia income tax returns. In short, non-itemizers in 1998 have no 1999 federal or state income tax reporting responsibilities with respect to their 1998 personal property tax refunds received in 1999.

Those taxpayers who were itemizers in 1998 should include their personal property tax refunds in gross income for 1999 to the extent of the tax benefit derived from the deduction of the personal property tax on the return for 1998. Taxpayers will include the full amount of the refund received in 1999 if the difference between the itemized deductions claimed on their 1998 federal income tax return and the applicable standard deduction for 1998 is *greater than* the amount of the refund received in 1999. If the difference between the itemized deductions claimed for 1998 and the applicable standard deduction is *less than* the amount of the refund received in 1999, then the taxpayer should only include such refund in gross income to the extent of the difference between the itemized deductions and the standard deduction for 1998. Here are some examples of this process:

Example 1:

Taxpayer A (single filing status) claimed itemized deductions totaling $4,350 for 1998 and received a personal property tax refund of $75 in 1999. The standard deduction for a taxpayer filing single status for 1998 is $4,250. Because the difference between the 1998 itemized deductions for Taxpayer A and his applicable standard deduction ($4,350 - $4,250 = $100) is **greater than** his personal property tax refund received in 1999 ($75), Taxpayer A would include his entire personal property tax refund ($75) in his gross income for 1999.

Example 2:

Taxpayers B and C (married filing joint status) claimed itemized deductions totaling $7,150 for 1998 and received a personal property tax refund of $75 in 1999. The standard deduction for taxpayers filing married jointly for 1998 is $7,100. Because the difference between the 1998 itemized deductions for Taxpayers B and C and their applicable standard deduction ($7,150 - $7,100 = $50) is **less than** the personal property tax refund received in 1999 ($75), Taxpayers B and C would only include $50 of such refund in their gross income for 1999.

High income taxpayers who are subject to the limitation of itemized deductions should follow Revenue Ruling 93-75, 1993-2 C.B. 63, issued by the Internal Revenue Service for calculating the proper includable amount of their personal property tax refund.

1999 Refunds of 1998 Taxes Paid in 1999

Taxpayers who pay their 1998 personal property tax after December 31, 1998, will have their refund check mailed within one hundred days of payment.

Those taxpayers who will be non-itemizers in 1999 should not include the amount of their 1999 personal property tax refunds of 1998 taxes when reporting income on their 1999 federal or Virginia income tax returns. In short, non-itemizers have no 1999 federal or state income tax reporting responsibilities with respect to their 1999 personal property tax refunds of 1998 taxes.

Those taxpayers who will be itemizers in 1999 should claim a deduction equal to the total amount of personal property tax paid less the amount of the refund received. For example, if a taxpayer pays $200 in 1999 for 1998 personal property taxes and receives a $25 refund in 1999, the taxpayer would be allowed a deduction of $175 on their 1999 federal income tax return. It is important to note that even though the assessment was made in 1998, the taxpayer would not be allowed a deduction in 1998 because the personal property tax was paid in 1999.

Tax Relief for 1999 and Thereafter

For 1999 tangible personal property taxes and thereafter, taxpayers' tangible personal property tax bills will be reduced by the amount of the tax relief provided by the Act. The taxpayer will be responsible for paying the tax shown as due on the bill.

Those taxpayers who will be non-itemizers in 1999 and thereafter have no income tax reporting responsibility with respect to the reduction in personal property tax shown on their personal property tax bill.

Those taxpayers who will be itemizers in 1999 and thereafter will only be allowed to deduct the amount of personal property tax actually paid. This will equal the total amount of tax shown on the bill minus the reduction shown on the bill.

IRS Private Letter Ruling

For a copy of the IRS Private Letter Ruling issued to the Commonwealth of Virginia concerning personal property tax refunds, you may either access the document on our web site at http:\\www.state.va.us\tax or you may request a copy from our Customer Services Section using the telephone number below.

If you have any questions regarding the income tax treatment of personal property tax refunds or need additional information, please contact the Department of Taxation as follows:

Virginia Department of Taxation
Customer Services Section
P.O. Box 1115
Richmond, VA 23218-1115

Phone (804)367-8098